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No. _____

Supreme Court, U.S.
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IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1988

JUDITH MORAN, *Petitioner*,

v.

CHARLES F. PERRY, *et al.*, *Respondents*.

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF WASHINGTON

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QUESTION PRESENTED

Does a state supreme court deny due process of law under the 14th Amendment in a civil case when it reverses the trial court's grant of an involuntary dismissal against a plaintiff and imposes liability on the defendant without affording the defendant an opportunity to prove an affirmative defense that is recognized by state law?

LIST OF PARTIES

The parties to the proceedings below were the petitioner Judith Moran and the respondents Charles F. Perry, Richard L. Whittemore, Randall L. Tanner, and Steven G. Shimizu; the respondents are a Washington partnership doing business under the name Perry, Whittemore & Tanner.

The respondents before this Court are the same as those appearing in the proceedings below.

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IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1988

JUDITH MORAN, *Petitioner,*

v.

CHARLES F. PERRY, *et al., Respondents.*

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF WASHINGTON

The petitioner Judith Moran respectfully prays that a writ of certiorari issue to review the judgment and opinion of the Supreme Court of Washington, entered in the above-entitled proceedings on January 19, 1989.

OPINIONS BELOW

The opinion of the Supreme Court of Washington for which review is sought is reported at 111 Wn.2d 885, 776 P.2d 1096 (1989); that decision is a reconsideration of the Washington Supreme Court's original opinion, which is reported at 109 Wn.2d 691, 748 P.2d 224 (1987). Both opinions are reprinted in the appendix hereto, pp. 1a and 53a, infra.

The Findings of Fact and Conclusions of Law of the Superior Court of Washington (Elston, J.) are reprinted in the appendix hereto, p. 70a, infra.

JURISDICTION

Respondents commenced this action in the Superior Court of Washington to enforce a contract claim against petitioner. In a bench trial, the court granted petitioner's motion for involuntary dismissal at the close of respondents' case. Respondents' appeal was certified directly to the Supreme Court of Washington, which on December 23, 1987, reversed the trial court's order of dismissal and remanded solely for the imposition of damages against petitioner.

Petitioner filed a timely motion for reconsideration before the Supreme Court of Washington, arguing inter alia that the order of remand constituted a denial of due process in that it precluded her from presenting proof of two affirmative defenses to the contract claim: (1) that

respondents had breached the contract, and (2) that the liquidated damages provision of the contract was unreasonable. By a decision on January 19, 1989, the Washington Supreme Court modified its earlier opinion in part, but remanded for the sole purpose of determining the issue of contract damages, thus barring petitioner from proving the affirmative defense of breach of contract by respondents.

The jurisdiction of this Court to review the judgment of the Supreme Court of Washington is invoked pursuant to 28 U.S.C. 1257(a).

Although further proceedings for the purpose of determining damages have been scheduled to commence in the Superior Court of Washington on September 28, 1989, this does not defeat the

jurisdiction of this Court.[1] The additional proceedings would only involve the question of the amount of damages to be imposed on petitioner, and this would have no effect on the federal issue in this case. See Cox Broadcasting Corp. v. Cohn, 420 U.S. 469, 477-480 (1975); Radio Station WOW v. Johnson, 326 U.S. 120, 124-27 (1945). Petitioner's affirmative defense of breach of contract, if proven, would entirely obviate the need for additional proceedings with respect to remedies. See p. 18, infra.

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[1] In view of the fact that trial on damages in this case will not be held during this Term of the Court, there would be ample time to stay the lower court proceedings in the event that this petition is granted.

STATUTE INVOLVED

28 U.S.C. 1257(a). State Courts; certiorari

(a) Final judgments or decrees rendered by the highest court of a state in which a decision could be had, may be reviewed by the Supreme Court by writ of certiorari where . . . any title, right, privilege, or immunity is specially set up or claimed under the Constitution or the treaties or statutes of, or any commission held or authority exercised under, the United States.

STATEMENT OF THE CASE

Respondents operated an accounting firm in the city of Seattle, Washington. Petitioner, a certified public accountant, was hired by respondents in 1981 as the manager of their retirement plan department. She was required by respondents to sign an employment agreement. The agreement contained a restrictive covenant that prohibited petitioner from providing services to any of respondents' client accounts for a period of five years after she left her employment with the firm. In addition, the covenant gave respondents the option of receiving 50% of the actual fees billed or billable by petitioner to any such client for a period of three years after the client first received services from petitioner.

Petitioner worked for respondents for one year, at which point she voluntarily resigned. Subsequently, she opened her own private accounting practice, specializing in the area of retirement plan accounting. In this new practice, petitioner's accounting services were requested by some of the former clients of respondents' firm. Petitioner advised respondents that she wished to perform work for those clients who had ceased their association with respondents' firm.

Respondents demanded that petitioner not provide accounting services for these clients. When petitioner refused the request, respondents filed this action in the Superior Court for King County, Washington, seeking injunctive relief against petitioner (at trial, respondents amended their complaint to seek damages as well). Petitioner answered by denying

that her actions constituted a breach of the agreement. Her answer also raised four affirmative defenses.

After a four-day bench trial, the Superior Court granted petitioner's motion for an involuntary dismissal at the close of the plaintiffs' case. The trial court found that petitioner had not solicited or diverted any of respondents' clients, and that no harm had resulted to respondents from the fact that petitioner had provided services to some of respondents' former clients. Further, the trial court ruled that the restrictive covenant was unreasonable to petitioner and harmful to the public. Accordingly, the Superior Court ordered the agreement modified to prohibit petitioner only from "soliciting or diverting" active clients of respondents. Because the court concluded that petitioner had done neither of these

things, directly or indirectly, it dismissed the complaint. See Findings of Fact Nos. 17-24, pp. 76a-78a, infra.

In its Findings of Facts, the Superior Court specifically noted that in view of the dismissal at the close of plaintiffs' case, the court made "no findings or conclusions as to the following defenses raised by the defendant: (a) the defense that the plaintiff has breached its implied covenant of good faith and fair dealing; and (b) the defense that the amount of liquidated damages contained in the liquidated damages clause of the Agreement is unreasonable and unenforceable." See Finding of Fact No. 28, p. 78a, infra.

The Supreme Court of Washington accepted review of the case and by a 5-4 majority reversed the decision of the Superior Court. The Court held that the

restrictive covenant was reasonable and enforceable as a matter of law. It also ruled that petitioner was obliged to pay 50% of any fees billed or billable to former clients of respondents pursuant to the liquidated damages provision in the contract. See pp. 34a-35a, infra. It remanded for proceedings consistent with the opinion.

Petitioner filed a timely motion for reconsideration in which she argued in part that the decision of the Washington Supreme Court constituted a denial of due process in that the terms of the remand precluded her from offering proof of the two affirmative defenses that had not been determined by the trial court. This was the stage in the proceedings in which the federal issue arose for the first time.

The Washington Supreme Court granted reconsideration and modified its earlier

opinion, but only with respect to the issue of liquidated damages. The majority opinion of the court did not mention the second outstanding affirmative defense interposed by petitioner, namely that respondents allegedly had breached the employment contract by failing to comply with express and implied conditions in the agreement. As to the issue of damages, the court noted that petitioner had not been given an opportunity to introduce evidence on the question, and consequently a remand was necessary for that purpose. The court then remanded the case to the Superior Court "for further proceedings to establish whether the sum set by the liquidated damages provision is reasonable and, if not, what sum is justified." See p. 59a, infra.

The dissenting opinion written by Justice Utter and joined by two other

members of the Washington Supreme Court focused on the failure of the majority to afford petitioner an opportunity to prove her defense. Characterizing this result as "a direct denial of due process," p. 69a, infra, the dissent opened with the following:

> I agree with the majority to the extent that it remands the case for determination of what liquidated damages are reasonable. However, I cannot agree that this court should resolve all of the remaining issues and dispose of the case. The unique procedural posture of the case precludes such action. We are not reviewing a completed trial; the trial court dismissed the case after plaintiff rested. Although the plaintiff spent 4 days presenting its case at trial, the defendant has never had the opportunity to present her evidence or to present any defense she may have. The trial court specifically reserved ruling on defendant's breach of contract defense. . . . The majority's revised opinion would remand only for determination of the reasonableness of damages, not Ms. Moran's defenses. This violates our own rules and the defendant's constitutional rights

to due process of law. Const. art 1, § 3; U.S. Const. amend. 14.

See pp. 59a-60a, infra.

REASONS FOR GRANTING THE WRIT

I.

The denial of an opportunity to prove affirmative defenses presents important questions of federal law that should be resolved by this Court

The Washington Supreme Court denied petitioner due process of law by deciding a case against her without allowing her an opportunity to prove affirmative defenses. As this Court has stated on numerous occasions, a fundamental aspect of the fourteenth amendment's guarantee of due process is that property may not be deprived except by an adjudication that provides an "opportunity for hearing appropriate to the nature of the case." Mullane v. Central Hanover Trust Co., 339 U.S. 306, 313 (1950). "Due Process

requires that there be an opportunity to present every available defense." Lindsey v. Normet, 405 U.S. 56, 66 (1972), quoting American Surety Co. v. Baldwin, 287 U.S. 156, 168 (1932). See also Goldberg v. Kelly, 397 U.S. 254, 267 (1970), quoting Grannis v. Ordean, 234 U.S. 385, 394 (1914) ("'The fundamental requisite of due process of law is the opportunity to be heard.'"); Griffin v. Griffin, 327 U.S. 220, 228 (1946) ("[T]o the extent that petitioner was thus deprived of an opportunity to raise defenses otherwise open to him under the law of New York, . . . there was a want of judicial due process. . . ."). Petitioner has been denied the right even to present legal authority in support of her position, much less the opportunity to introduce evidence to establish her defense. At least "'some form of hearing' is required before the

owner is finally deprived of a protected property interest." Logan v. Zimmerman Brush Co., 455 U.S. 422, 433 (1982), quoting Board of Regents v. Roth, 408 U.S. 564, 570-71 (1972) (emphasis in original). "[A] hearing in its very essence demands that he who is entitled to it shall have the right to support his allegations by argument however brief, and, if need be, by proof, however informal." Londoner v. City and County of Denver, 210 U.S. 373, 386 (1908).

The legal sufficiency of a defense is determined by state law; likewise, states may impose reasonable requirements for pleading defenses. However, once the state has recognized a property interest in the form of a defense to a contract claim, the adequacy of the procedures provided for determining the validity of the defense are controlled by the due process clause of the fourteenth

amendment. See Cleveland Board of Education v. Loudermill, 470 U.S. 532, 541 (1985); Logan v. Zimmerman Brush Co., 455 U.S. at 432; Vitek v. Jones, 445 U.S. 480, 490-91 & n.6 (1980).

Petitioner raised her affirmative defenses in a timely fashion by pleading them in her answer. See Wash. Super. Ct. R. 8(b)-(c). Washington courts utilize a notice pleading system that is patterned after the Federal Rules of Civil Procedure; the statement of an affirmative defense need only advise the plaintiff of the general position of the pleader. See Trautman, Pleading Principles and Problems in Washington, 56 Wash. L. Rev. 687, 694 (1981). After properly pleading an affirmative defense, the defendant is entitled to prove facts consistent with the general theory of the defense. See, e.g., Pearson v.

Vandermay, 67 Wn.2d 222, 230-33, 407 P.2d 143, 148-49 (1965).

Under Washington law, a material breach of contract by one party discharges the duty of the other party to perform. See Jacks v. Blazer, 39 Wn.2d 277, 284-85, 235 P.2d 187, 191 (1951); Dwinell's Central Neon v. Cosmopolitan Chinook Hotel, 21 Wn. App. 929, 937, 587 P.2d 191, 195 (1978). Such breaches may be based on either express or implied conditions in contracts. See Thompson v. St. Regis Paper Co., 102 Wn.2d 219, 229, 685 P.2d 1081, 1087 (1984) (employer bound by provisions in employee handbooks); Fuller Market Basket, Inc. v. Gillingham & Jones, Inc., 14 Wn. App. 128, 133-34, 539 P.2d 868, 871-72 (1975) (implied covenants).

Respondents never challenged petitioner's defense of contract breach in the Superior Court. Washington civil

procedure permits a plaintiff to do so by a motion to strike a defense that is insufficient as a matter of law, see Wash. Super. Ct. R. 12(f), or by a motion for summary judgment. See Wash. Super. Ct. R. 56. The trial court unmistakably concluded that the defense had been preserved: the court specifically noted that it was not reaching the affirmative defenses interposed by petitioner. See Finding of Fact No. 28, p. 28a, infra. On appeal, the affirmative defense of contract breach was not discussed by any party until petitioner moved for reconsideration of the Washington Supreme Court's initial decision. There was no opportunity on appeal to argue the merits of the defense; rather, the question was whether petitioner had a right to offer proof of the defense on remand.

Under the terms of the remand order in this case, petitioner will be

precluded from offering any defense except as it applies to the issue of liquidated damages. Upon entry of judgment in the case, her defenses will merge in the judgment and she will be barred by res judicata rules from asserting them in a later proceeding. See Mellor v. Chamberlin, 100 Wn.2d 643, 645-46, 673 P.2d 610, 611-12 (1983); Stallcup v. City of Tacoma, 13 Wash. 141, 147, 42 P. 541, 543 (1895), appeal dismissed, 165 U.S. 719 (1897).

The failure to provide petitioner with any forum for proving her defenses violates "the two central concerns of procedural due process, the prevention of unjustified or mistaken deprivations and the promotion of participation and dialogue by affected individuals in the decisionmaking process." Marshall v. Jerrico, Inc., 446 U.S. 238, 242 (1980). A process that does not "consider the

merits, . . . based upon the substantiality of the available evidence," runs the grave risk of depriving persons of property "in a random manner." Logan v. Zimmerman Brush Co., 455 U.S. at 434.

The action of the Washington Supreme Court in this case was an arbitrary departure from established Washington practice. As Justice Utter pointed out in his dissent, Washington procedure limits an appellate court's review of a dismissal at the close of plaintiff's case to ascertaining whether there was sufficient evidence to make out a prima facie case for the plaintiff. See p. 61a, infra. Furthermore, the Washington Supreme Court has previously held that on remand following such a reversal the defendant must have an opportunity to put on affirmative defenses. In Lonsdale v. Chesterfield,

91 Wn.2d 189, 191, 588 P.2d 217, 219 (1978), the court observed that if this practice were not followed, "[a] defendant would run an unacceptable risk of having a motion to dismiss granted by the trial court only to lose on the merits at the appellate level without ever having had an opportunity to present his case."

Petitioner realizes that it is not the business of this Court to enforce the procedural rules of state courts. Yet in this case the Washington Supreme Court abandoned a longstanding practice on an apparently ad hoc basis. Had petitioner known that the appellate court would preclude the defense, she surely would have avoided moving for dismissal at trial until after she put on her own case. Commentators have noted that a principal purpose of the due process clause is to assure regularity in

procedures in order to provide a basis for rational behavior on the part of those affected by state action. See L. TRIBE, AMERICAN CONSTITUTIONAL LAW 629-32 (2d. ed. 1988).

II.

The decision below denying petitioner an opportunity to prove an affirmative defense conflicts with the decisions of this Court, other state courts of last resort and federal courts of appeals

The decision of the Washington court departs from the practice followed in other state and federal courts. Ordinarily the appellate reversal of a trial court's dismissal of a complaint is accompanied by a remand for the purpose of allowing the defendant to proceed with the presentation of any available defenses. See 5 J. MOORE, FEDERAL PRACTICE ¶41.13[2], at 41-170-171 (1988). This Court insisted that defendants be afforded such an opportunity in United

States v. United States Gypsum Co., 340 U.S. 76, 85 (1950). State courts and lower federal courts have required similar protection for defendants. See, e.g., Riegel Fiber Corp. v. Anderson Gin Co., 512 F.2d 784, 793 (5th Cir. 1975); Bowles v. Biberman Bros., Inc., 152 F.2d 700, 705 (3d Cir. 1946); Gulbenkian v. Gulbenkian, 147 F.2d 173, 177 (2d Cir. 1945); Bogle v. Potter, 68 N.M. 239, 360 P.2d 650, 654-55 (1961); Reiter v. Illinois Nat'l. Casualty Co., 397 Ill. 141, 73 N.E.2d 412, 414-15 (1947).

None of these decisions were based expressly on the command of the due process clause. But as the argument in the previous section demonstrates, the standard practice in American courts is rooted in the due process consideration that a defendant is entitled to be heard on all legally recognized defenses. The Illinois court cited above remarked that

"absurd consequences" would follow from precluding the defendant's proof, 73 N.E. 2d at 415; likewise the Fifth Circuit stressed that "the defendants must of course be allowed to present their evidence." Riegel Fiber Corp. v. Anderson Gin Co., 512 F.2d at 793.

CONCLUSION

For the reasons stated, this petition for certiorari should be granted.

Respectfully submitted,

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APPENDIX

No. 52944-2. En Banc.

CHARLES F. PERRY, ET AL, Appellants, v.

JUDITH MORAN, Respondent

[1] Master and Servant -- Contracts -- Covenant Not To Compete -- Validity -- Prohibition Against Providing Services. A covenant not to compete may prohibit an employee upon termination of employment from providing services for a reasonable time to parties who had been clients of the former employer. The scope of a covenant not to compete need not be limited to prohibiting the solicitation or diversion of the former employer's clients.

[2] Master and Servant -- Contracts -- Covenant Not To Compete --

Validity -- Test. A covenant not to compete is valid if it is reasonable, i.e., if it is necessary to protect the employer's business or goodwill, its scope is no greater than reasonably necessary to accomplish this protective purpose, and its enforcement would not cause undue injury to the public.

[3] Master and Servant -- Contracts -- Covenant Not To Compete -- Reformation. A valid covenant not to compete is not subject to judicial modification.

[4] Master and Servant -- Contracts -- Covenant Not To Compete -- Liquidated Damages -- Validity. A liquidated damages provision in a covenant not to compete, i.e., a requirement that a former employee

> pay damages according to a specific formula if he chooses to engage in business with the clients of his former employer, is valid if the damages specified are reasonably related to the expected harm.

Utter, J., Pearson, C.J., Brachtenbach, J., and Schumacher, J. Pro Tem., dissent by separate opinion; Goodloe, J., did not participate in the disposition of this case.

Nature of Action: An accounting firm sought liquidated damages from its former employee or an injunction prohibiting her from providing accounting services to clients of the firm. The defendant's employment agreement contained a noncompetition covenant which, upon her terminating employment, prohibited her from servicing clients of

the firm for a period of 5 years or, if she chose to service such clients, required her to pay one-half of the fees earned from those clients for a period of 3 years.

Superior Court: The Superior Court for King County, No. 82-2-16408-9, Robert M. Elston, J., on July 30, 1984, dismissed the action at the close of the plaintiff's case and awarded the defendant attorney fees.

Supreme Court: Holding that the terms of the covenant not to compete were reasonable and enforceable, the court reverses the judgment and grants judgment in favor of the plaintiff.

Tousley, Brain, Reinhardsen & Block, by William H. Block and Christopher I. Brain, for appellants.

Lucas, Glase, Sherman & Hendrickson, Peter J. Lucas, and Merrilee A. MacLean, for respondent.

CALLOW, J.--The plaintiff, Perry, Whittemore and Tanner (PWT) is a Seattle accounting firm. In 1981, the firm consisted of 4 partners, 18 or 19 staff accountants, and 25 to 30 support employees. The firm was organized into three basic departments, including the Retirement Department for which the defendant, Judith Moran, was hired.

The defendant, Moran, began her career as an accountant in Michigan in 1972, performing retirement plan work. In 1976, she left the company she was working for to start her own practice in the same area, taking a major part of her initial client base from among her first employer's clients with the employer's

consent. Moran practiced on her own in Michigan from 1976 to 1980, when she sold her practice.

After selling her Michigan accounting practice, Moran moved to Seattle, where she took a position with City College as an administrator and teacher of accounting. She did not develop an accounting practice in Seattle during the time she was employed with City College.

In June of 1981, Moran accepted a position with PWT as the head of its Retirement Department. At the time she began working for PWT, Moran executed an employment agreement, which included the following provisions:

> Section 5. Non-Competition.
>
> 5.1 Clients. Employee recognizes and acknowledges that all clients and/or accounts serviced by Employer, Employer's other employees, or Employee during his employment with Employer, including all

clients and/or accounts acquired by Employee due to his efforts, are the clients and accounts of Employer (collectively "Client Accounts").

5.2 Non-Disclosure. Employee recognizes and acknowledges that the list of Employer's Client Accounts, as it may exist from time to time, is a valuable, special and unique asset of the Employer's business. Employee shall not, during or at any time after the term of his employment, disclose the list of Client Accounts or any part thereof to any person, firm, corporation, association, or other entity for any reason or purpose whatsoever.

5.3 Restrictive Covenant. In the event this Agreement is terminated by either party, Employee shall not, either individually or as an employee or principal of another accounting or business firm, provide services to any Client Accounts within a five-year (5) period immediately subsequent to his termination of employment.

5.4 Additional Remedy. If for any reason Employee shall (i) acquire or otherwise obtain from Employer, by any means whatsoever, Client Accounts or provide services to such Client Accounts, then at the sole

> election of employer, Employee shall pay to Employer fifty percent (50%) of the actual fees billed or billable to such Client Accounts by Employee each year for a period of three (3) years commencing with the date Employee first renders services to such Client Accounts.
>
> Payment will be remitted to Employer by Employee with [sic] fifteen (15) days after collection of amounts billed by Employee to Client Accounts, or within sixty (60) days of billing by Employee to Client Accounts, whichever comes first. If services rendered by Employee to Client Accounts are provided on an on-going basis of sixty (60) days or longer, progress payments will be made by Employee to Employer at (60)-day intervals based on progress billings by Employee to Client Accounts.
>
> The foregoing remedy shall be in addition to any other remedies provided to Employer hereunder or by law.

Moran was employed with PWT for slightly more than 1 year. Under her supervision, the PWT Retirement Department was comprised of herself, Robert Ellis, a senior staff accountant,

and Ruth Wett, an administrative staff member. Together they provided services that centered on the preparation of returns and filings related to retirement plans and defined benefit plans for professional service corporations.

Because of the nature of the PWT Retirement Department's work, much of its accountant-client contact came through clients, attorneys or outside general accountants. During her employment with PWT, Moran met a number of PWT clients and intermediaries.

On August 15, 1982, Moran gave notice of her intent to leave PWT, and on October 14, 1982, she terminated her employment. Shortly thereafter, Ellis and Wett also left PWT and joined Moran in a combined practice offering services similar to those performed by the PWT Retirement Department.

Soon after leaving PWT, Moran mailed notices of her new business to numerous individuals and companies who might offer client referrals. About 6 months later, she sent copies of a brochure describing her accounting practice to another list of people. While no notices or brochures were sent to actual PWT clients, some were sent to intermediaries of PWT clients who Moran had met while employed at PWT. The client intermediaries whom Moran contacted referred clients to her, including some who had been PWT clients during Moran's employment with PWT. During the 17 months between the time Moran left PWT and trial, she performed over $78,000 worth of services for clients who had been PWT clients during her employment with PWT.

Upon learning that Moran was servicing former PWT clients, PWT requested that she pay liquidated damages

in accordance with section 5.4 of the employment agreement. When she refused, PWT filed the present action seeking either an injunction prohibiting Moran from servicing PWT client accounts or damages.

Trial commenced in June 1984. At the close of PWT's case, Moran moved for dismissal and the court granted the motion. The trial court based its determination in part on the following findings of fact:

> 16. Certain of the clients for whom Judith Moran provides accounting services are individuals or companies which had been clients of PWT, but had left PWT some time prior to being referred to Judith Moran. Some had left PWT prior to October 15, 1982, and others had left after October 15, 1982.
>
> 17. At no time did Judith Moran, directly or indirectly, solicit any active client of PWT.
>
> 18. At no time did Judith Moran, directly or indirectly,

divert from PWT the accounting business of any active client of PWT.

19. No harm has resulted to PWT by the fact that former clients of PWT have sought and received accounting services from Judith Moran, as opposed to other accountants or accounting firms.

20. The effort to restrict Judith Moran from servicing clients who have already left PWT and are not active clients of PWT is a restraint which is greater than that which is reasonably necessary for the protection of the business or goodwill of PWT.

21. The effort to restrict Judith Moran from servicing clients who have already left PWT and are not active clients of PWT results in a degree of restriction of the public which is unnecessary, unwarranted and unreasonable.

22. The restrictive provisions of the Employment Agreement are unreasonable and should be modified so that they are reasonable and lawful.

23. Given the facts of this case, the restrictive provisions of the subject Employment Agreement should be modified so that Judith Moran would only be restricted from "soliciting or

> diverting" active clients of PWT.
>
> 24. In that there is no evidence that Judith Moran solicited or diverted active clients of PWT, plaintiffs' claims for damages and injunctive relief should be denied, and the preliminary injunction entered herein should be dissolved.

The trial court, in the judgment signed July 30, 1984, stated, inter alia:

> The Employment Agreement between the parties herein executed on the 25th day of September, 1981, is modified and reformed in all respects, including those clauses relating to remedies, so that the restrictive provisions contained therein restrict Judith Moran only from "soliciting or diverting active clients of PWT" through October 14, 1987.

The trial court also awarded Moran attorneys' fees in the amount of $34,948.60.

The "findings of fact" entered by the trial court are to a great extent irrelevant to the issues presented. The

case involves a contract of employment freely entered into between the parties and understood by the employee. The "findings of fact" by the trial court are, in reality, a rewriting of the agreement by the trial court and a stating of new terms for the agreement in the form of conclusions of law. The parties could contract that in return for employment the employee would agree that for a reasonable time she would not "provide services" to employer's clients. This is the heart of the agreement approved in Racine v. Bender, 141 Wash. 606, 252 P. 115 (1927), and Knight, Vale & Gregory v. McDaniel, 37 Wn. App. 366, 680 P.2d 448, review denied, 101 Wn.2d 1025 (1984). These decisions support the prohibition against the performance of services so that an employer can protect its client base without the necessity of proving the

solicitation or diversion of clients (an evidentiary morass at best) but need only prove that the client of the employee had been the client of the former employer.

This case involves an attempt by an accounting firm, doing primarily accounting services for doctors and clinics, to protect its client base from a defecting employee to whom it has introduced those clients. It involves an employee who after only approximately 14 months employment, long enough to ingratiate herself with the firm's clients, departs with an entire department and ends up with a number of those clients. It involves an employment agreement that specifies liquidated damages for the protection of the employer if the employee takes all or a portion of the employer's business.

The issue in this case is whether the trial court should have dismissed an

action to enforce an accountant's covenant not to provide services to clients of a former employer after terminating employment or, in the alternative, to pay as liquidated damages 50 percent of any fees charged for services rendered to the former employer's clients for a period of 3 years. We hold that such a covenant is consistent with Racine v. Bender, supra, and is valid and enforceable. The trial court erred in dismissing the claim.

Racine v. Bender, supra, and Knight, Vale & Gregory v. McDaniel, supra, involve restrictive covenants as applied to employees of accounting firms. The circumstances of both cases are similar to the present case. In each of the three cases the employee signed a covenant not to perform work for clients of the former employer, but after leaving the employing firm, did perform work for

those clients. In both Racine and Knight, the courts enforced the covenants as written. Neither court required a showing that the former employee had solicited the employer's former clients.

In Racine, the court upheld an employee's covenant which provided, in pertinent part:

> "(d) For a period of three years after leaving such employment I will not:
> "(1) Solicit accounting or auditing work from any person, firm or corporation with whom I came in contact as a representative of Samuel F. Racine & Co., or
> "(2) Perform any accounting or auditing work, either acting for myself or for any other party, for any person, firm or corporation with whom I came in contact during my employment with Samuel F. Racine & Co. . . ."

(Italics ours.) Racine, at 607.

The Racine opinion stated that:

> Roughly construed, these provisions prohibit respondent from soliciting or doing, within a period of three years, any work for any of those

> people whose desire for his services comes because through his work as a representative of the appellant he was enabled to acquire a knowledge of their business, or become intimate with the members of the staff of such business. . . . In the broadest sense, the restriction is nothing more than to prohibit respondent from taking appellant's clients with him when he severs his connection with appellant, or to perform services for those so intimately connected with such clients as to be fairly classified as his future clients. That such a requirement so accords with common honesty between men, and a failure to observe it leads to such direful results, is so well established that it seems strange that it should be contended that one engaged in a position where confidence is the basis of the relation between client and the employee and that confidence results through the employer and is the foundation stone of his business, then the employee may, disregarding his employer's rights, visit ruin upon him. The general rule applied in construing such contracts, is that restrictions therein are upheld, if they meet the test of showing that they are not greater than are reasonably necessary to protect the business or good will of

> the employer, even though they restrain the employee of his liberty to engage in a certain occupation or business, and deprive the public of the services, or restrain trade.

(Italics ours.) Racine, at 610-11.

In 1984, the 3-part test for reasonableness of a covenant established in Racine was stated again in Knight, Vale & Gregory v. McDaniel, supra at 369, as follows:

> Whether a covenant is reasonable involves a consideration of three factors: (1) whether restraint is necessary for the protection of the business or goodwill of the employer, (2) whether it imposes upon the employee any greater restraint than is reasonably necessary to secure the employer's business or goodwill, and (3) whether the degree of injury to the public is such loss of the service and skill of the employee as to warrant non-enforcement of the covenant.

Applying this test the court found reasonable a covenant prohibiting the employee from performing work for the employer's former clients for a period of

3 years. The court upheld the granting of summary judgment to the employer stating:

> Absent disputed facts, the construction or legal effect of a contract, including the "reasonableness" of a covenant not to compete, is determined by the court as a matter of law. Marquez v. UW, 32 Wn. App. 302 648 P.2d 94 (1982); Alexander & Alexander, Inc. v. Wohlman, 19 Wn. App. 670, 684, 578 P.2d 530 (1978). The primary dispute between the parties concerns enforceability of the warranty agreement and the reasonableness of its covenant not to compete. The facts surrounding entering into the agreement and the acts constituting violation of the covenant are undisputed. Therefore, resolution of the issue by summary judgment was appropriate. Yeats v. Estate of Yeats, 90 Wn.2d 201, 204, 580 P.2d 617 (1978).

Knight, at 368. The court enforced the covenant's provision for liquidated damages of 35 percent of fees billed or billable to those clients within the 3-year period with the following observations.

> Turning to the question of liquidated damages, the general rule is that such damage clauses are favored and are enforceable if they do not constitute a penalty or are otherwise unlawful. The test for enforceability of liquidated damages is (1) the amount fixed must be a reasonable forecast of just compensation for the harm that is caused by the breach, and (2) the harm must be such that it is incapable or very difficult of ascertainment. Harm resulting to one business from the competition of another business is difficult to estimate accurately. Here, however, there was an expert's uncontroverted affidavit that the damages sought of 35 percent of any fees collected reflect no more than a reasonable forecast of the harm to the employer occasioned by a breach of the covenant. Because the formula is based upon a percentage of competing business actually occurring it is directly linked to the actual damage to goodwill experienced by the employer. In addition, the 35 percent figure is based upon a general formula in the accounting field for purchase of an ongoing practice. In short, the clause is not an arbitrary estimate of damages, is not a penalty and is enforceable.

(Citations omitted.) Knight, at 371-72. See also Wood v. May, 73 Wn.2d 307, 438 P.2d 587 (1968); Columbia College of Music & Sch. of Dramatic Art v. Tunberg, 64 Wash. 19, 116 P. 280 (1911).

When one examines the actions of the defendant in this case under the light of the principles established by Wood v. May, supra; Racine v. Bender, supra; Knight, Vale & Gregory v. McDaniel, supra; and Sheppard v. Blackstock Lumber Co., 85 Wn.2d 929, 540 P.2d 1373 (1975), those principles can only be upheld or the opinions reversed.

We find Judith Moran's covenant not to perform accounting work for PWT clients to be proper, reasonable and enforceable. PWT has a legitimate interest in protecting its existing client base from depletion by a former employee. It had a justifiable expectation that if it provided

employment to an accountant, that employee would not take its customers. A covenant prohibiting the former employee from providing accounting services to the firm's clients for a reasonable time is a fair means of protecting that client base. A bargain by an employee not to compete with the employer during the term of employment or thereafter for a reasonable time and within a reasonable territory, as may be necessary for the protection of the interests of the employer without imposing undue hardship on the employee, is valid. Restatement of Contracts § 516(f) (1932). Such covenants encourage employment of accountants by accounting firms and they discourage the taking of the employer's clients without preventing the employee from engaging in the profession. Wolf & Co. v. Waldron, 51 Ill. App. 3d 239, 366 N.E.2d 603 (1977); Faw, Casson & Co. v.

Cranston, 375 A.2d 463 (Del. Ch. 1977); 15 A.L.R.4th 559.

One unpleasant alternative for accounting firms and other employers who rely upon covenants not to compete to protect their business, if such covenants are not upheld, is to forever rotate the employees who service clients with other employees, thereby limiting employee client contact as much as possible. Another unattractive alternative is constant management supervision or monitoring of the employee's work so that the client looks always to management rather than the employee for answers. It is readily apparent that forcing such courses of conduct upon an employer is costly, inefficient and would lead to unsatisfactory firm-client relationships. No rule of law should force employers into such actions.

The defendant and the trial court suggest that PWT could adequately protect its client base by merely prohibiting a former employee from soliciting or diverting those clients from the employer. However, such a covenant would not adequately safeguard the employer's interest in retaining its clients. A covenant that merely prohibits solicitation or diversion places upon the employer the burden of proving (1) that the former employee performed some act or acts which had the potential of enticing clients away from the employer, and (2) that those acts were the cause of the client's decision to leave the employer and seek accounting services from the former employee. If this burden were placed upon an employer, the process would be difficult and expensive. The employer would be required to invest time and money in litigating the nature of the

former employee's actions toward the clients. In many cases the employer would have to bring those clients into the litigation as witnesses to prove that solicitation occurred. Particularly where, as here, those clients are doctors, clinics and business corporations, an attempt to involve the clients in litigation would damage the goodwill existing between those clients and the employer, and would damage the reputation of the employer with potential clients. A prudent employer could not rely on such a covenant to protect its client base. It is reasonable for the employer to preclude the employee from servicing those who were clients of the employer during the period of employment and for a period after the cessation of employment.

The alternative would be for the employer to require employees to covenant

not to practice accounting in the geographical area served by the employer. Such a covenant would be more restrictive upon the former employee, since it would require the former employee to either establish a practice outside the geographical region with which he had become familiar during his employment, or to forgo practicing accounting entirely for the period of time covered by the covenant. A covenant not to compete within a geographical area places greater restrictions on the employee than does a covenant not to service the former employer's client accounts.

> The essential purpose of the post-employment restraint . . . is not to prevent the competitive use of the unique personal qualities of the employee--either during or after the employment--but to prevent competitive use, for a time, of information or relationships which pertain peculiarly to the employer and which the employee acquired in the course of the employment.

Blake, Employee Agreements Not To Compete, 73 Harv. L. Rev. 625, 647 (1960). In addition, covenants not to compete within a particular geographical area open up the employer to vexatious litigation to establish whether a court deems the size of the geographical area to be reasonable and litigation from the standpoint of the employer is to be avoided if possible.

A feasible alternative is proposed in a Seton Hall Law Review:

> The rules of the law that surround restrictive covenants strive to achieve a balance between the rights and duties of contending interests. By restricting the accountant covenantee from rendering professional services to clients of his or her former firm, the court is within the ambit of the traditional rules of restrictive covenant law although there may be some adverse effect on the public; that is, those clients who would prefer to enjoy the continued services of the accountant leaving the firm. That effect, however, is

> avoided or lessened if instead of granting injunctive relief, the court requires the former employee or partner to pay for the clients "taken." By providing the purchase price and terms in the agreement, the court's task is made easier and the likelihood of enforcement is enhanced. Thus, the legitimate interest of the employer is protected without imposing undue hardship on the employee or being overly injurious to the public.

Pachman, Accountants and Restrictive Covenants: The Client Commodity, 13 Seton Hall L. Rev. 312, 322 (1983). The PWT-Moran covenant achieves the balance advocated by Pachman. By prohibiting Moran from providing any accounting services to PWT clients, the agreement clearly defines what actions are prohibited, making litigation unnecessary in most cases. Where litigation is necessary to enforce the covenant, the issue is limited to whether services were performed for the employer's clients which can be proven by producing billing

records, making it unnecessary to involve clients in the litigation process. At the same time, the PWT-Moran covenant leaves Moran free to compete with PWT for new clients in the same geographical area. Indeed, the covenant even allows Moran to serve PWT clients, if she is willing to return one-half of her fees to PWT for a period of 3 years. This covenant is less restrictive than the covenant upheld in Racine, which was enforced by enjoining the former employee from servicing former clients of the employer, without an option to pay damages for the privilege of taking the clients.

Moran cites Wood v. May, 73 Wn.2d 307, 438 P.2d 587 (1968) to justify the trial court's modification of the covenant in this case. We recognize that a trial court has the power to modify a covenant so that it may be enforced to

some extent, rather than invalidating the covenant entirely. However, such a modification is proper only where the original covenant is unenforceable. Here the original covenant was reasonable and should be enforced as written.

It is also proposed that restriction of competition for 5 years is perhaps too long and is therefor unreasonable. It is suggested that the cause should be remanded to the trial court for determination of that issue. We see no reason to adopt that proposal. First, the period of time between the defendant's leaving employment and trial was only 17 months. The 5 year period of restriction may have been too long a period of time but, in any event, the duration of the period has become irrelevant to the disposition of this case. The 5 year period restricting competition was not enforced by the trial

court or germane to either the issue of violation of the covenant or the issue of damages. It may be that a clause forbidding service for a 5 year period is unreasonable as a matter of law, but here, where the employee left the employment in October of 1982 and proceeded during the next year and a half to service the employer's clients, and that period is all that is involved in this litigation, and the employer has not sought damages beyond those computable at the time of trial; the length of the period, even if excessive, is immaterial. A remand on this issue would unfairly and unnecessarily impose upon the employer additional costly, burdensome litigation that the employment contract was designed to avoid.

The defendant contends that even if the covenant not to serve PWT clients is enforceable, the amount of liquidated

damages for violation of the covenant is excessive. In Knight, the court upheld a liquidated damages clause requiring a former employee to pay 35 percent of fees billed or billable to a client of the employer or a total of 105 percent of annual fees. During the trial evidence was admitted that PWT was purchasing the right to service former clients of another accounting firm for a total of 135 percent of the annual fees billed to these clients. Since PWT voluntarily entered into this agreement, it was relevant to show that the percentage of fees to be paid under the covenant was reasonably within the range of fees normally paid by accounting firms for the right to service certain accounts. In her employment agreement, Judith Moran agreed not to service PWT client accounts, or if she did service the accounts, to pay 50 percent of the fees

billed or billable to those accounts for a period of 3 years, or a total of 150 percent of the one year's fees. The record contains substantial testimony that this is a reasonable price to pay for permanently acquiring a client. There is testimony that others had entered into similar agreements and had paid liquidated damages in the same range for performing services for clients of prior employers. There was evidence that the liquidated damage provision in this agreement was typical of similar clauses in other employment agreements in the Seattle-Tacoma area.

We find that the amount owing for these accounts is within the range of reasonable agreements for the transfer of the right to service accounts. Isler v. Shuck, 38 Or. App. 233, 589 P.2d 1180 (1979). We reject the approach of Smith, Batchelder & Rugg v. Foster, 119 N.H.

679, 406 A.2d 1310, 15 A.L.R.4th 551 (1979). Whether a covenant not to compete is reasonable and enforceable or has been violated cannot be based upon the respective incomes or a comparison of the size of the parties involved or the amount of the damage suffered.

It follows that Moran, the former employee, should pay the ex-employer, Perry, Whittemore and Tanner, 50 percent of any fees billed or billable to former PWT accounts for a period of 3 years following her termination of employment with PWT.

The dismissal and the trial court's award of attorney's fees to the defendant are reversed. Judith Moran's covenant not to perform accounting services for PWT client accounts or, if such services were performed, to pay PWT 50 percent of any fees billed to those accounts for 3 years, is valid and enforceable. The

cause is remanded to the trial court for further proceedings consistent with this opinion. See Alexander & Alexander, Inc. v. Wohlman, 19 Wn. App. 670, 578 P.2d 530 (1978). The award of attorney's fees for both trial and appellate representation shall abide the final disposition of the case. RAP 18.1(e)

DOLLIVER, DORE, ANDERSEN, and DURHAM, JJ., concur.

UTTER, J. (dissenting)--This case concerns the reasonableness and enforceability of an employment contract's restrictive covenant and liquidated damages provision. In holding the noncompetition covenant reasonable and enforceable as written, the majority fails to consider the covenant's terms, ignores the trial court's findings of fact, and rules contrary to this state's general policy disfavoring contracts in restraint of trade. In addition, the

primary cases relied on by the majority do not support the result reached. Unlike the majority, I agree with the trial court that the covenant's terms were more restrictive than necessary to protect the employer's business and goodwill. However, I find the trial court's covenant modifications unreasonable and would alter them accordingly. As to the enforceability of the liquidated damages provision, on which the trial court did not entertain evidence or rule, I think it inappropriate for this court to decide a factual matter without a remand to the trial court. Because I would reach a result different from the majority, I must dissent.

Well established public policy in Washington disfavors contracts in restraint of trade. See, e.g., RCW 19.86.030; Organon, Inc. v. Hepler,

23 Wn. App. 432, 436 n.1, 595 P.2d 1314 (1979). This court has repeatedly recognized that covenants not to compete constitute contracts in restraint of trade. Wood v. May, 73 Wn.2d 307, 308-09, 438 P.2d 587 (1968); Racine v. Bender, 141 Wash. 606, 611, 252 P. 115 (1927). Consequently, we enforce such covenants only to the limited extent that they constitute partial restraints and meet the test of reasonableness. Sheppard v. Blackstock Lumber Co., 85 Wn.2d 929, 931, 540 P.2d 1973 (1975); Wood, at 308. To further the public policy disfavoring restraints of trade, we should carefully examine and narrowly construe all covenants not to compete. See Knight, Vale & Gregory v. McDaniel, 37 Wn. App. 366, 370, 680 P.2d 448, review denied, 101 Wn.2d 1025 (1984).

Essentially, the majority concludes that the challenged covenant "-is valid

and enforceable" because it "is consistent with Racine . . ." Majority, at 6. To the extent that Racine recognized that an accounting firm had a legitimate interest in protecting its existing client base, I agree with the majority. However, the validity of the covenant's specific restrictions depends in part upon whether the restrictions "are not greater than are reasonably necessary to protect the business or good will of the employer . . ." Racine, at 611. If this court intends to continue adhering to the approach adopted in Racine and Wood, the reasonableness of each specific restriction must be tested under the particular circumstances of each case as demonstrated by the evidence presented. Sheppard, at 933; Wood, at 312.

The majority never discusses the covenant's specific terms. The

restrictive covenant in question forbids Ms. Moran for 5 years from servicing any clients who were clients of Perry, Whittemore & Tanner (PWT) during her term of employment. I believe both the scope of the service restriction and its duration to be in conflict with Racine and Wood, and not reasonably necessary to protect PWT's business or good will.

We have found service restrictions reasonable in general, and particularly so in the accounting context, because it would be natural for a client to shift its accounting business from an employer's firm to follow a trusted accountant with whom it has a working relationship and who has valuable knowledge of the client's business and internal operations. Racine, at 612-13; Knight, at 370. Service restrictions are intended to prevent the employee from gaining unfair advantage from his or her

knowledge of, or acquaintance with, the former employer's clients. Racine, at 611; Wood, at 310. Here, Ms. Moran worked not as a general accountant, but rather in the very specialized PWT Retirement Department, which serviced a limited number of PWT clients. Report of Proceedings II, at 136, 207. Yet, the service restriction extends to all clients serviced by the various PWT departments. Even as to Retirement Department clients, the restriction applies regardless of whether Ms. Moran had gained specific knowledge of the client's accounting needs and regardless of whether she had any contact with the client or a party closely identified with the client. Consequently, despite the majority's unsupported conclusion, the PWT service restriction conflicts with the covenants upheld in Racine and Knight, both of which were limited to

clients with which the employee had come in contact. Racine, at 607; Knight, at 369. Moreover, the restriction covers clients who terminated their relationship with PWT prior to Ms. Moran's leaving, as well as clients that had taken all of their accounting work to other firms, and later decided to have Ms. Moran handle their retirement plan work. Findings of fact 16, 20; Clerk's Papers, at 5-6.

Based upon these facts, the trial court concluded that the service restriction was greater than that reasonably necessary to protect PWT's business and goodwill. Conclusions of law 5, 6; Clerk's Papers, at 7. I find the trial court's conclusions supported by substantial evidence, and uncontroverted by the majority opinion, which concentrates its analysis solely on the reasonableness of the trial court's modification and the liquidated damages provision.

The majority also failed to consider the reasonableness of the 5-year period during which the service restriction continues to apply. Although the trial court reached no conclusion concerning the service restriction's duration, I would find 5 years unreasonable as a matter of law. See Wood, at 311. Presumably, the restriction's duration should reflect the time PWT needs to reestablish a client-accountant relationship, independent from the departing employee. Ms. Moran's term of employment lasted approximately 1 year. Findings of fact 5, 7; Clerk's Papers, at 4. Yet for the covenant to be reasonable, this court must be convinced that PWT needs 5 years to reestablish client trust. Albeit in a different context, we held in Wood that a 5 year duration was unreasonable for an employee's covenant not to compete with

his employer. Rather than dictating a reasonable time period, I would follow the procedure established in Wood, where we remanded for the trial court to determine whether "1 year, 3 years or some other period of time is reasonable under the facts in this case." Wood, at 312. I would note in passing, that Racine and Knight approved 3 year covenants, but given that retirement accounting is cyclical, consisting mostly of tax filings, Report of Proceedings III, at 391-96, a two or three tax return limit may be more appropriate in this case.

Having found the covenant unreasonable, the trial court modified the restrictive provision so that Ms. Moran would only be restricted from "soliciting or diverting" active clients. Clerk's Papers, at 6, 8. I agree with the majority's conclusion that while the

trial court had authority to modify, the covenant as modified "would not adequately safeguard the employer's interest in retaining its clients." Majority, at 10. When an employee leaves an employer, especially in the accountant context, clients would often choose to follow, not because of solicitation or diversion, but because of the nature of their relationship with, and the confidential knowledge of, the employee. As this court observed in Racine, clients do not desire the departing employee's services because he or she is the only person who has the ability to perform them, "but because they know him [or her] well and he [or she] knows all about their business." Racine, at 612-13.

I would require the trial court to modify the covenant so that Ms. Moran would be prohibited from servicing clients about whom she had gained

confidential information or who she served previously as a PWT employee. The modified covenant would be subject to two exceptions: (1) clients that affirmatively and independently terminated their relationship with PWT prior to Ms. Moran's leaving; or (2) clients that left after Ms. Moran to have their entire accounting needs serviced by an accountant other than PWT, and subsequently transferred their retirement accounting to Ms. Moran. To address the majority's concern with the fairness of PWT' burden of proof, I would require Ms. Moran to demonstrate that a particular client covered by the covenant comes within one of the exceptions. With these modifications, I believe the covenant can protect PWT's legitimate interest, without imposing undue hardship on Ms. Moran and without injuring the

public's interest. See Racine, at 611-12; Knight, at 369.

Finally, I must also disagree with the majority's treatment of the liquidated damages provision. Under the employment contract, if Ms. Moran serviced clients in violation of the covenant, she would have to pay PWT 50 percent of her billings to the client for 3 years, or a total of 150 percent of the annual fees. Because the trial court ruled immediately after PWT presented its case, Ms. Moran had no opportunity to present evidence on the reasonableness of the 150 percent requirement and the trial court entered no findings and made no ruling on the issue. Finding of fact 28; Clerk's Papers, at 7. In fact, the trial court precluded Ms. Moran's counsel from exploring the reasonableness of the 150 percent figure during cross examination

of PWT witnesses. Report of Proceedings II, at 270-73.

Nevertheless, the majority has concluded that 150 percent of annual fees "is within the range of reasonable agreements for the transfer of the right to service accounts." Majority, at 15. I think the majority's conclusion is both inappropriate and inaccurate for several reasons. The majority relies on Knight where the court found 105 percent of annual fees reasonable. Knight, at 372. However, in Knight the parties had litigated the issue. There, the court based its decision on expert opinion in the record, which established 105 percent as a reasonable forecast of harm to the employer and as based on a general formula in the accounting field for purchases of an ongoing practice. Knight, at 371-72. By contrast, here the majority relies on a single piece of

evidence culled from the record, demonstrating that PWT recently purchased the right to service accounts for 135 percent of annual fees. Majority, at 14. By basing its determination of reasonableness not on objective market information, but on what PWT has paid, the majority works an injustice on Ms. Moran, who has never had the opportunity to litigate the issue.

I also think the 150 percent figure inappropriate because it is based on the amount Ms. Moran bills each year for 3 years, rather than on the amount PWT billed prior to losing its client. As the Knight court recognized, the amount of liquidated damages must be "a reasonable forecast of just compensation for the harm that is caused by the breach . . ." Knight, at 371. I think it relevant that PWT, in purchasing client accounts from other firms, limits

its payments to a percentage of what the seller firm billed the client, rather than a percentage of what PWT bills in the future. Report of Proceedings III, at 407-11; Ex. 17.

Because this case concerns a restrictive covenant, I think it also appropriate to ensure that the liquidated damage provision does not impose an undue hardship on the employee. Thus, I agree in principle with the New Hampshire approach enunciated in Smith, Batchelder & Rugg v. Foster, 119 N.H. 679 406 A.2d 1310, 1313 (1979). However, I also agree with the majority, when it rejects certain specific considerations used by the New Hampshire court, such as the respective incomes and comparative sizes of the parties. Majority, at 15. Instead, I would limit the amount paid by Ms. Moran in any one year to no more than a reasonable percentage of the amount

billed by PWT in the last year it serviced the client. In this way, PWT would be compensated for the harm it suffered, while any additional business generated by Ms. Moran's efforts would be protected. As I have indicated, the reasonableness of the 150 percent figure should be left to the trial court to determine after the parties have had a full opportunity to litigate the issue.

In summary, the majority has failed to recognize that the covenant's terms conflict with those approved in Racine, Wood, and Knight. By also failing to recognize the essentially factual nature of the inquiry required, the majority has acted inconsistently with our approach set down in Racine and Wood. Moreover, by failing to remand the issue of the liquidated damages provision, the majority does a great injustice both to Ms. Moran and to our adversarial fact

finding procedures. Consequently, I must dissent.

PEARSON, C.J., BRACHTENBACH, J., and SCHUMACHER, J. Pro Tem., concur with UTTER, J.

Reconsideration granted June 9, 1988.

Opinion of the Washington Supreme Court
(January 19, 1989)

No. 52944-2. En Banc.

CHARLES F. PERRY, ET AL, Appellants, v.

JUDITH MORAN, Respondent.

[1] Damages -- Liquidated Damages -- Validity -- Enforcement. A liquidated damages clause is favored and will be enforced if the amount fixed is a reasonable forecast of just compensation for the harm caused by the breach and the harm is such that it is incapable or very difficult of ascertainment.

[2] Master and Servant -- Contracts -- Covenant Not To Compete -- Liquidated Damages -- Validity. The harm caused by a breach of a covenant not to compete is difficult to measure and a liquidated damage provision is appropriate for such an agreement.

Utter, Brachtenbach, and Pearson, JJ., dissent by separate opinion.

Nature of Action: An accounting firm, asserting a breach of a covenant not to compete, sought liquidated damages from a former employee or an injunction prohibiting her from providing accounting services to clients of the firm.

Superior Court: The Superior Court for King County No. 82-2-16408-9, Robert M. Elston, J., after modifying the noncompetition clause and finding no breach thereof, entered a judgment on July 30, 1984, in favor of the defendant.

Supreme Court: Upon reconsideration of its prior decision reported at 109 Wn.2d 691, the court adheres to its prior opinion except for the last four

paragraphs thereof. Holding in this opinion that there had been no determination of breach of the covenant not to compete, in the form agreed to by the parties, the court reverses the judgment and remands for a determination of whether the liquidated damages are reasonable and, if not, what sum is justified.

Tousley, Brain, Reinhardsen & Block, by William H. Block and Christopher I. Brain, for appellants.

Lucas, Glase, Sherman & Hendrickson, Peter J. Lucas, and Merrilee A. MacLean, for respondent.

Marvin L. Gray, Jr., and Samuel Saracino on behalf of Moss Adams and Hagen, Kurth, Perman & Co., amici curiae for appellants.

CALLOW, C.J.--Upon reconsideration of Perry v. Moran, 109 Wn.2d 691, 748 P.2d 224 (1987), we affirm our earlier holding with one modification. We delete the last four paragraphs of the opinion as reflected in the earlier report and substitute therefor the following:

The defendant contends that even if the covenant not to serve Perry, Whittemore and Tanner (PWT) clients is enforceable, the amount of liquidated damages for violation of the covenant is excessive. The liquidated damages clause calls for Moran to pay PWT for a 3-year period 50 percent of the amount she bills former clients to whom she has provided services in violation of the covenant not to compete.

Washington law favors the enforcement of a liquidated damages clause. As stated in Management, Inc. v.

Schassberger, 39 Wn.2d 321, 326, 235 P.2d 293 (1951):

> We are loathe to interfere with the rights of parties to contract as they please between themselves, and the fact that the parties to a contract call a sum stipulated to be paid in case of breach of the contract liquidated damages is a circumstance to be given serious consideration in determining whether it is in fact liquidated damages.

A liquidated damages clause will be enforced if the amount fixed is a reasonable forecast of just compensation for the harm caused by the breach and the harm is such that it is incapable or very difficult of ascertainment. Walter Implement, Inc. v. Focht, 107 Wn.2d 553, 559, 730 P.2d 1340 (1987). The harm caused by the breach of a covenant not to compete is very difficult to accurately quantify. Walter Implement Co., 107 Wn.2d at 559; Knight v. McDaniel, 37 Wn. App. 366, 371, 680 P.2d 448 (1984); Mead

v. Anton, 33 Wn.2d 741, 756, 207 P.2d 227 (1949). Here, the trial court heard sufficient evidence to support the conclusion that the liquidated damages amount was a reasonable forecast of just compensation for the harm. We would have no difficulty affirming its decision had the trial court held the clause enforceable.

However, because of its determination that Moran had not violated the terms of the covenant as erroneously modified, the trial court made no determination as to the reasonableness of the liquidated damages clause. Moreover, the defendant has not been permitted to introduce evidence on this issue. Therefore, it would be premature for this court to determine the enforceability of the liquidated damages clause.

The dismissal and the trial court's award of attorney's fees to the defendant

are reversed. Judith Moran's covenant not to perform accounting services for PWT client accounts is valid and enforceable. The cause is remanded to the trial court for further proceedings to establish whether the sum set by the liquidated damages provision is reasonable and, if not, what sum is justified. See Alexander & Alexander, Inc. v. Wohlman, 19 Wn. App. 670, 578 P.2d 530 (1978). The award of attorney's fees for both trial and appellate representation shall abide the final disposition of the cause. RAP 18.1(e).

DOLLIVER, DORE, ANDERSEN, DURHAM, and SMITH, JJ., concur.

UTTER, J. (dissenting)--I agree with the majority to the extent that it remands the case for determination of what liquidated damages are reasonable. However, I cannot agree that this court should resolve all of the remaining

issues and dispose of the case. The unique procedural posture of the case precludes such action. We are not reviewing a completed trial; the trial court dismissed the case after plaintiff rested. Although the plaintiff spent 4 days presenting its case at trial, the defendant has never had the opportunity to present her evidence or to present any defense she may have. The trial court specifically reserved ruling on defendant's breach of contract defense. Finding of fact 28. The majority's revised opinion would remand only for determination of the reasonableness of damages, not Ms. Moran's defenses. This violates our own rules and the defendant's constitutional rights to due process of law. Const. art. 1, § 3; U.S. Const. amend. 14.

On appeal from a judgment granting dismissal made at the close of

plaintiff's case, our review is limited to determining whether there was sufficient evidence to establish a prima facie case for the plaintiff. See Spring v. Department of Labor & Indus., 96 Wn.2d 914, 918, 640 P.2d 1 (1982); Schmidt v. Pioneer United Dairies, 60 Wn.2d 271, 272, 373 P.2d 764 (1962); Richards v. Kuppinger, 46 Wn.2d 62, 278 P. 2d 395 (1955). In our review of a judgment of dismissal made before the defendant has presented any evidence, we cannot summarily dispose of the entire case. Court rules specifically provide that a defendant's motion to dismiss after plaintiff rests may be made "without waiving his right to offer evidence in the event the motion is not granted . . ." CR 41(b)(3); See 4 L. Orland, Wash. Prac., Rules Practice § 5502 (3d ed. 1983 & Supp. 1988). The

majority's action is contrary to our established law and procedures.

Aside from the question of possible defenses, the reasonableness of a covenant not to compete can be determined as a matter of law only if there are no disputed facts. See Knight, Vale & Gregory v. McDaniel, 37 Wn. App. 366, 368, 680 P.2d 448, review denied, 101 Wn.2d 1025 (1984) hereafter KVG). Factual analysis is critical. General rules are not possible because each case "must be decided on its own particular set of facts. All of the circumstances must be taken into account . . ." (Footnote omitted.) 11 S. Williston, Contracts § 1447, at 1024 (3d ed. 1968); Wood v. May, 73 Wn.2d 307, 312, 438 P.2d 587 (1968). Therefore we must determine which facts are critical and whether we have all the critical facts before this court.

Professor Williston provides guidance in the process of discussing one court's thorough and "outstanding" inquiry into the reasonableness of a covenant not to compete. S. Williston, at §§ 1447, 1643A (discussing Arthur Murray Dance Studios of Cleveland, Inc. v. Witter, 105 N.E.2d 685 (Ohio C.C.P. 1952) (where the plaintiff sought an injunction)). In determining whether the restraint was greater than reasonably necessary to protect the employer, the Witter court posed 41 "trenchant" questions, among them:

> "12. Did employee's work give him opportunity to become acquainted with employer's customers?
>
> "13. How many of employer's customers did employee come to know?
>
> "14. Was this particular employee practically the employer's sole and exclusive contact with the customer?
>
> "15. Was employee's contact with employer's customers a regular, re-occurring contact?

> "16. Was employee's contact with employer's customers a close, personal, direct and ingratiating contact that gave employee such a hold on customers that they would follow him to the rival?

(Footnotes omitted.) S. Williston, § 1447, at 1028-29 (noting that the court buttressed each question with ample citations). Although no one question is conclusive on the issue of reasonableness, each highlights a circumstance or fact of the case that should be considered.

The emphasis on confidentiality is also consistent with the general principal/agent axioms. The Restatement holds an agent accountable for "profits made by the sale or use of trade secrets and other confidential information . . ." Restatement (Second) of Agency § 396(c)

(1958).[1] Some commentators would restructure judicial analysis of covenants not to compete by eliminating reference to contract law and focusing entirely on agency principles. See Closius & Schaffer, Involuntary Nonservitude: The Current Judicial Enforcement of Employee Covenants Not to Compete -- A Proposal for Reform, 57 S. Cal. L. Rev. 531 (1984). Under such analysis, the only supportable inquiry involves the extent to which the employee has gained and is using confidential information. See generally Closius & Schaffer, 57 S. Cal. L. Rev. 531.

Consistent with both the traditional contract approach and the proposed agency approach, our own cases suggest that confidentiality factors must be

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[1] The Restatement imposes the duty whether or not the agent competes with the principal.

considered. See Racine v. Bender, 141 Wash. 606, 252 P. 115 (1927); KVG. The courts in both Racine and KVG, stressed the importance of the accountant's "confidential knowledge . . . of all the important and vital matters concerning the [client's] business." Racine, at 608.

> [T]he evidence showed that the business of a certified public accountant is such that *the person who actually performs the labor incident thereto* acquires an intimate knowledge of the business of the client, preparing audits of the business, income tax returns, and other matters very *confidential* in their nature, and vital to the business itself.

(Italics mine.) Racine, at 608. The language in KVG is similar:

> This [business] interest is enhanced in the sphere of public accounting because the nature of the accountant-client relationship is such that employees of such a firm gain extensive, valuable knowledge of the clients' business and internal operations and develop a close, familiar working relationship with the client.

37 Wn. App. at 370. The confidentiality element would give a terminating accountant a distinct competitive advantage against her former firm.

The covenants in both Racine and KVG restricted the accountant from performing services for persons with whom the accountant came into contact while an employee of the firm. Racine, at 607, 610; KVG, at 369. The latter court stressed the proviso:

> In this case, KVG has sought enforcement of the covenant only as it pertains to performing accounting services during the 3-year period for only those former clients of KVG with whom defendants came into contact as a direct result of their employment. To this extent, we find

> that the covenant is reasonable and lawful.

KVG, at 370.[2]

In contrast, the covenant in the present case prevents Moran from servicing any former PWT client, whether or not she had any contact with that account while an employee of PWT. The covenant is broader than those recognized as reasonable in our previous decisions. The majority offers no justification for departing from previous analysis, but rather calls the cases "consistent." Perhaps the majority finds consistency by assuming that, as head of the retirement department, Ms. Moran must have had

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[2] The court specifically disclaimed approving the entire covenant, citing possible problems with overbreadth. The questionable provisions prohibited performing work for "(1) 'any person, firm or corporation with whom I come in contact . . .', and (2) 'members of the staffs of your clients as well as occupants of their offices. . . .'" 37 Wn. App. at 370, n.1.

confidential information about every client that might seek her services after she left PWT. We cannot assume these facts as she has not yet presented her defense. Moran claims she neither met nor serviced the accounts of some of the PWT clients while she was employed there. Report of Proceedings, at 381. She also claims that the evidence will show that although she was the manager of the retirement department, her authority and treatment were not commensurate with her title. Report of Proceedings, at 404. Because Ms. Moran has had no opportunity to present evidence regarding these facts, which should be part of the reasonableness analysis, we must remand this issue to the trial court. Failure to do so would be a direct denial of due process.

BRACHTENBACH and PEARSON, JJ., concur with UTTER, J.

Findings/Conclusions by Superior Court of Washington (July 30, 1984)

IN THE SUPERIOR COURT OF THE STATE OF

WASHINGTON IN AND FOR KING COUNTY

CHARLES F. PERRY, RICHARD L. WHITTEMORE, RANDALL L. TANNER and STEVEN G. SHIMIZU, d/b/a PERRY, WHITTEMORE & TANNER, a Washington partnership,	)	No. 82-2-16408-9
Plaintiffs,	)	FINDINGS OF FACT AND CONCLUSIONS OF LAW
v.	)	
JUDITH MORAN,	)	
Defendant.	)	

THIS MATTER having come on before the above-entitled court for trial from the 26th day of June, 1984, through the 29th day of June, 1984, before the Honorable Judge Robert M. Elston, plaintiffs appearing through Charles F. Perry and Randall L. Tanner, and being represented by their attorney, Christopher I. Brain of Haggard, Tousley & Brain, and the defendant Judith Moran appearing individually, and being

represented by her attorney, Peter J. Lucas of Lucas, Glase & Chicoine. The Court being fully advised in the premises, at the conclusion of the plaintiffs' case, makes its:

FINDINGS OF FACTS

1. Plaintiffs are general partners of Perry, Whittemore & Tanner, a Washington general partnership, engaged in the professional practice of public accounting, with principal offices located in Seattle, Washington. (Plaintiffs are hereafter collectively referred to as "PWT".)

2. The defendant Judith Moran is a certified public accountant and resident of King County, Washington.

3. On August 3, 1981, Judith Moran commenced employment with PWT, as the manager of the retirement plan department.

4. Prior to her commencing employment, Judith Moran was advised she would be required to sign an Employment Agreement, and was given a copy of an Employment Agreement then in use by PWT. She was advised that the Agreement was in the process of minor revision. Sections 5.1 and 5.3 (the restrictive provisions at issue) were not revised.

5. After commencing employment, Judith Moran was given the final draft of an Employment Agreement, which she read carefully and thereafter sent to Robert Condie, an attorney friend, for his comment. On September 25, 1981, Judith Moran and representatives of PWT executed that document. The executed document shall hereafter be referred to as the "Employment Agreement".

6. The term of the Employment Agreement called for employment on a month-to-month basis. Either party had

the right to terminate the Agreement upon 60 days written notice to the other.

7. On August 15, 1982, Judith Moran provided notice to PWT that she would voluntarily terminate her employment on October 15, 1982.

8. Judith Moran was continuously employed at PWT from August 3, 1981, through October 15, 1982, as the manager of the PWT retirement plan department.

9. When she was hired by PWT, Judith Moran had skill and expertise as an accountant and had developed skills in the speciality area of retirement plan accounting. Judith Moran was also skilled as a manager, having left a position as the manager of the accounting and finance department for City College, to take employment with PWT.

10. The Employment Agreement contains a restrictive covenant in paragraph 5.3 which purports to restrict

Judith Moran so that she may not "provide services to any Client Accounts within a five year period immediately subsequent to his [sic] termination of employment." "Client Accounts" as defined by paragraph 5.1 of the Employment Agreement includes only those clients serviced by PWT during the time Judith Moran was employed.

11. On leaving the employ of PWT, Judith Moran opened an accounting office in the Fremont District, in north Seattle on October 18, 1982.

12. Upon opening her accounting office, Judith Moran mailed a notice of her new business to numerous individuals and companies who would be likely to give referrals, none of which were then active clients of PWT.

13. Approximately six months after establishing her accounting office, Judith Moran prepared a brochure, which

brochure stressed the positive aspects of her practice, and in no way detracted from, or reflected poorly on, PWT.

14. Judith Moran's accounting practice generally specializes in providing accounting services related to the maintenance and qualification of pension and profit sharing plans. The corporations which maintain the pension and profit sharing plans generally have accountants, or accounting firms, other than Judith Moran, who function as the principal accountant and business advisor to the client.

15. The clients serviced by Judith Moran are referred to her by third parties, which include attorneys, insurance people, or the accountants who deal with those clients and serve as that client's principal accountant and business advisor.

16. Certain of the clients for whom Judith Moran provides accounting services are individuals or companies which had been clients of PWT, but had left PWT some time prior to being referred to Judith Moran. Some had left PWT prior to October 15, 1982, and others had left after October 15, 1982.

17. At no time did Judith Moran, directly or indirectly, solicit any active client of PWT.

18. At no time did Judith Moran, directly or indirectly, divert from PWT the accounting business of any active client of PWT.

19. No harm has resulted to PWT by the fact that former clients of PWT have sought and received accounting services from Judith Moran, as opposed to other accountants or accounting firms.

20. The effort to restrict Judith Moran from servicing clients who have

already left PWT and are not active clients of PWT is a restraint which is greater than that which is reasonably necessary for the protection of the business or goodwill of PWT.

21. The effort to restrict Judith Moran from servicing clients who have already left PWT and are not active clients of PWT results in a degree of restriction of the public which is unnecessary, unwarranted and unreasonable.

22. The restrictive provisions of the Employment Agreement are unreasonable and should be modified so that they are reasonable and lawful.

23. Given the facts of this case, the restrictive provisions of the subject Employment Agreement should be modified so that Judith Moran would only be restricted from "soliciting or diverting" active clients of PWT.

24. In that there is no evidence that Judith Moran solicited or diverted active clients of PWT, plaintiffs' claims for damages and injunctive relief should be denied, and the preliminary injunction entered herein should be dissolved.

25. The subject Employment Agreement contains a provision that the prevailing party should be awarded reasonable attorney fees and costs.

26. The defendant is a married woman, but has maintained her accounting business as her separate property, and all rights and liabilities in this action are the separate property of Judith Moran.

27. Plaintiffs' motion to amend its complaint to include a cause of action for liquidated damages was granted at the outset of the trial.

28. In that the findings above referenced have been entered by this

court at the conclusions of plaintiffs' case, this court makes no findings or conclusions as to the following defenses raised by the defendant: (a) the defense that the plaintiff has breached its implied covenant of good faith and fair dealing; and (b) the defense that the amount of liquidated damages contained in the liquidated damages clause of the Agreement is unreasonable and unenforceable.

CONCLUSIONS OF LAW

1. This court has jurisdiction over the parties and the subject matter of this action.

2. The parties executed an Employment Agreement on September 25, 1981.

3. Sole consideration for the Employment Agreement was the continued employment of Judith Moran by PWT.

4. What restrictive provisions in an employment agreement are reasonably necessary to protect the legitimate business interests of an employer is dependent upon the facts of each case.

5. Based upon the facts of this case, the restrictive provisions of the Employment Agreement are unreasonable, overbroad and overly restrictive.

6. The restrictive provisions contained in the Employment Agreement are greater than those which are reasonably necessary to protect the business and goodwill of the plaintiff.

7. The restrictive provisions contained in the Employment Agreement violate the rights of former clients and result in a degree of restriction to the public which is unnecessary and unwarranted.

8. The restrictive provisions of the Employment Agreement are

unreasonable, overbroad, and overly restrictive in that they apply without qualification to all clients of PWT during Judith Moran's employment and prevent her from later providing services to those clients without regard to whether: (a) she had no knowledge of, or no contact with, those clients while she was at PWT; or (b) those clients had left PWT before Judith Moran left PWT; or (c) Judith Moran did not solicit or divert those clients away from PWT.

9. This court has the authority to modify the restrictive provisions of the Employment Agreement so that they are reasonable and lawful.

10. The restrictive provisions of the Employment Agreement should be modified so that Judith Moran shall only be restricted from "soliciting or diverting" active clients of PWT.

11. In that Judith Moran has not, directly or indirectly, solicited or diverted active clients of PWT, plaintiffs' complaint for injunctive relief should be dismissed, plaintiffs' amended complaint for liquidated damages should be dismissed and the preliminary injunction entered herein should be dissolved.

12. Judith Moran as the prevailing party is entitled to judgment against plaintiffs in the amount of $34,948.60 for reasonable attorneys fees and costs incurred herein.

13. In that the counterclaim of the defendant asks for attorney fees by way of damages, and in that the defendant is awarded attorney fees as a prevailing party, the defendant's counterclaim should be dismissed.

DONE IN OPEN COURT this 30th day of July, 1984.

(signature)
The HONORABLE JUDGE
ROBERT M. ELSTON

Presented by:

LUCAS, GLASE & CHICOINE

(signature)
Peter J. Lucas
Attorneys for Defendant

Copy Received and Notice of Presentation Waived:

HAGGARD, TOUSLEY & BRAIN

(signature)
Christopher I. Brain
Attorneys for Plaintiffs

Order of Washington Supreme Court granting reconsideration (June 9, 1984)

THE SUPREME COURT OF WASHINGTON

CHARLES F. PERRY, ET AL,	)	No. 52944-2
Appellants,	)	ORDER GRANTING MOTION FOR RECONSIDER-ATION CALLING FOR NEW ARGUMENT
v.	)	
JUDITH MORAN,	)	
Respondent.	)	

The Court having decided by majority vote that the respondent's motion for reconsideration should be granted,

It is ordered that the motion be and it hereby is granted, and that the cause be set for rehearing En Banc at a later date.

Dated this 9th day of June, 1988.

Vernon R. Pearson (signature)
Chief Justice

109 Wn.2d 691

Mandate of Washington Supreme Court
(February 8, 1989)

THE SUPREME COURT OF WASHINGTON

CHARLES F. PERRY, RICHARD L. WHITTEMORE, RANDALL L. TANNER, and STEVEN G. SHIMIZU, d/b/a PERRY, WHITTEMORE & TANNER, a Washington partnership,	)	No. 52944-2
Appellants,	)	MANDATE King County No. 82-2-16408-9
v.	)	
JUDITH MORAN,	)	
Respondent.	)	

The State of Washington to:

The Superior Court of the State of Washington in and for King County

This is to certify that the opinion of the Supreme Court of the State of Washington filed on January 19, 1989, became the decision terminating review of this court in the above entitled case on February 8, 1989. This cause is mandated to the superior court from which the appeal was taken for further proceedings

in accordance with the attached true copy of the opinion.

Pursuant to Rule of Appellate Procedure 14.3, costs are taxed as follows: $4,486.35 awarded to Appellants and against Respondent.

IN TESTIMONY WHEREOF, I have hereunto set my hand and affixed the seal of said Court at Olympia, this 9th day of February, A.D. 1989.

(signature)
C. J. MERRITT
Clerk of the Supreme Court,
State of Washington

cc: Mr. William Block
Mr. Christopher Brain
Mr. Peter Lucas
Ms. Merrilee MacLean
Mr. John Plymyer
Mr. Marvin Gray, Jr.
Mr. Samuel Saracino
Reporter of Decisions